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Venezuela: Economics and the Oil Picture

Massive oil revenues are helping spur economic growth, despite the decline of oil production since the 1973-74 oil price hikes. Public investment is growing rapidly as the government pursues its $27 billion 1976-80 development program in metals, petrochemicals, and infrastructure. Venezuela has earmarked $6 billion for oil exploration and development, but expenditures are lagging. To reverse declining oil reserves, Venezuela will have to accelerate and increase oil investment.

Economic growth is being maintained at about 6 percent under the impetus of the investment program. Consumption is being further bolstered by high government expenditures for wages, welfare programs, and subsidies. Soaring imports and extensive price controls are nevertheless holding the lid on inflation again this year, despite some food shortages resulting from last year's

Venezuela: Major Economic Indicators

	1970	1971	1972	1973	1974	1975	1976
				Percent Change			
Real GDP growth	2.4	4.5	3.6	5.8	4.5	6.2[1]	6.0[1]
Inflation	3.3	3.2	2.9	4.1	8.3	10.3	7.0
				Billion US $			
Exports (f.o.b.)	2.6	3.0	3.1	4.6	11.1	8.7	8.8
Imports (f.o.b.)	1.7	1.9	2.2	2.6	3.9	5.5	6.5
Trade balance	0.9	1.1	0.9	2.0	7.2	3.2	2.3

[1] Estimated.

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Venezuela: Indicators of Oil Activity

	Oil Production (Million b/d)	Number of Wells Completed		
		Total	Total Exploratory	Exploratory in New Areas
1970	3.7	622	37	1
1971	3.5	601	44	2
1972	3.2	496	62	12
1973	3.4	420	59	9
1974	3.0	407	110	7
1975	2.3	281	34	1
1976	2.3	339	38	0
1977	NA	NA	60[1]	NA

[1] Planned.

poor crop. Venezuela's inflation rate is well below those of most other OPEC countries; the cost of living index increased at an annual rate of about 8 percent, just under the 1974-76 average.

Caracas thus far is financing much of its investment program with foreign borrowing while attempting to keep its estimated $8.5 billion foreign reserves intact. The government has already borrowed $2.3 billion in Euro-currency and Eurobond markets in the past nine months and probably hopes to obtain as much as $1.1 billion more later this year. Even so, Venezuela may well incur a small payments deficit this year comparable to a $200 million shortfall in 1976. The deficits reflect a reduction in the current-account surplus caused by rising imports and net capital outflows generated by foreign aid and compensation payments for the nationalized oil and iron ore industries. Venezuela achieved a $4.1-billion payments surplus in 1974.

The Nationalized Oil Industry

Since nationalization on January 1, 1976, current oil operations have gone smoothly, in large part because the former owners are helping to run the industry under

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technical service and marketing contracts. At 2.3 million barrels per day (b/d), oil output is below capacity but slightly above planned conservation levels of 2.2 million b/d. So far this year, exports have not been adversely affected by Venezuela's position on the high side of the OPEC dual price system. Oil sales are handled largely by the former owners, although Petroven, the government oil holding company, is selling 20 percent of oil exports on its own account. To streamline industry operations this year, the 14 former operating companies under Petroven have been consolidated into 9.

Exploration and development efforts since nationalization have reportedly been a disappointment to President Perez. In the first year of government ownership, investment outlays amounted to $500 million, less than half the planned amount. Exploration efforts remained near the low levels of company drilling in the last year of private ownership, and oil reserves fell 3 percent during the year to 14 billion barrels.

President Perez has upgraded Petroven's status by transferring responsibility for development of the Orinoco Tar Belt to it from the conservationist-dominated Ministry of Energy and Mines. With this expression of confidence, Petroven is likely to become more influential in determining oil policy. Planned investment levels this year, however, reflect only moderately greater exploration and investment activity. In April, Caracas announced that $700 million would be invested this year, well below the previous figure of $820 million. Specific goals include raising productive capacity by reworking inactive wells and increasing secondary recovery. In this connection, Petroven has shut in some wells to avoid flaring of associated gas. Most exploration will involve evaluation of areas bordering currently operating fields.

Compensation Problems

Relations with the foreign oil companies are somewhat strained because the government has failed to pay full compensation on schedule. More than half of the nearly $1 billion in compensation bonds is still being held by Venezuela in the guarantee fund set up to ensure that the companies properly maintained oil facilities prior to nationalization. The funds will not be released

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until final review of field evaluations of production equipment, pipelines, refineries, and settlement of back tax claims. Asset deductions are estimated to average 25 percent of the deposits in the fund, but some range as high as 55 percent.

Government claims for back taxes could further reduce final compensation. The comptroller general has filed a claim against the companies' deposits totaling more than $500 million, and additional tax claims have been made by the Ministry of Finance. The comptroller general's claim probably will have to be decided by the Venezuelan Supreme Court. Despite assurances from the Energy Ministry that the claim has little or no legal basis, foreign companies have yet to win a significant tax case before the Supreme Court.

President Perez promises to resolve compensation problems by the end of this year, but further delays are still likely. The Supreme Court probably will not be able to act on the comptroller's tax claim before the present congressional session ends in July. Since the October-December session is traditionally set aside for the budget, congressional approval for release of the guarantee fund is unlikely this year and would be difficult to obtain during next year's presidential campaign. Moreover, Finance Minister Hurtado fears that release of the bonds from the guarantee fund will saturate international markets for Venezuelan issues.

Outlook Through 1980

Paced by public investment, economic growth is likely to continue during 1978-80 at much the same pace as this year. Caracas plans to keep oil production near current levels. Strong aggregate demand will spur industrial production, and a return to normal weather should restore agricultural output. Some upward pressure on prices will likely persist despite large continuing gains in imports.

Venezuela's balance of payments will come under increasing pressure. The current account will probably slip into deficit in 1978, and deficits will likely grow rapidly through 1980 if--as expected--the real price of oil remains constant. Expected government borrowing of

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$1 billion to $2 billion annually in the Eurocurrency market should bring the capital account into approximate balance over the period. Consequently, Caracas probably will have to draw $5-6 billion from foreign reserves through 1980.

Caracas plans to boost oil investment to $1.6 billion annually in 1978-80, although inflation and the high cost of deep and offshore drilling probably will require additional funds. Investment will be devoted to accelerating exploration, maintaining production capacity, and altering refineries to process the country's increasingly heavier crude. Exploration in promising but difficult offshore areas and development of the Orinoco are scheduled to receive greater emphasis. Venezuela hopes to find 6 billion barrels of oil during the 1976-80 period--a net increase to proved reserves of about 2 billion barrels at current production levels.

Finding and developing new reserves will require increased participation by foreign oil firms. Venezuela is unable to develop independently the sophisticated technology necessary to exploit offshore areas and the Orinoco. Moreover, without the companies' managerial assistance continued slippage in investment schedules is likely.

The future role of foreign oil companies remains in doubt. Unless Caracas becomes more generous with compensation, the companies may be reluctant to increase their participation. In any case, Venezuela wants to maintain political and economic independence, and the political tensions arising from the December 1978 presidential election campaign will prevent Caracas from seeking expanded foreign involvement during the next two years.

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In the long run, substantially increasing recoverable reserves will depend on success in developing the Orinoco Tar Belt. Some $86 million is being spent this year on the initial phases of a three-year, $1.2 billion project. Although the Tar Belt is estimated to contain up to 700 billion barrels of oil, only a small fraction is recoverable with existing technology at current prices. [redacted] 25X1

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Peru: Protests Over Economic Program Growing

Reaction has been growing in Peru to the tough austerity program recently announced by the government to meet International Monetary Fund requirements for providing the aid Peru needs to meet debt-service obligations.

The program includes 50-percent increases in gasoline prices, a one-third hike in public transportation fares, and a $200-million cut in imports this year. Central government expenditures, including those of the military, will be reduced by 8 percent or $160 million. The Peruvian sol is to be devalued by about 20 percent in a series of steps to be completed by the end of the year.

The program failed to provoke the strong, spontaneous public protest initially expected by the government. Last week, however, violent leftist student demonstrations in Cuzco prompted officials to clamp a dusk-to-dawn curfew on that ancient city. The student demonstrations have since spread to Lima and Arequipa. No large-scale worker protests have as yet materialized.

The stringent internal security measures in effect and Finance Minister Piazza's sketchy description of the program may have helped dampen initial reaction. The announcement of modest wage increases probably also contributed. Mass demonstrations could still occur once Peruvians feel the pinch of higher prices for food, gasoline, and transportation, for which government subsidies were removed.

Piazza's program meets many, but not all, of the conditions set last March by the IMF for a $100-million standby loan badly needed by Peru. Successful negotiation of the loan is a prerequisite for another $300 million in balance-of-payments support loans from foreign banks. It is not clear whether the IMF will be satisfied with the measures.

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Cuba-Ethiopia: Military Advisers

There are now about 65 Cuban military personnel in Ethiopia, [redacted] 25X1 Their most important role is advising Ethiopian military planners on the use of Soviet equipment, but they are also serving as advisers to Ethiopian instructors who are training the Peoples Militia. Despite earlier reports, the number of Cuban military personnel in Ethiopia may not increase significantly above the present level.

Cuban concern about the deteriorating situation in Angola may have led to a decision to limit the number of advisers sent to Ethiopia for the time being. [redacted] 25X1 25X1

Additional nonmilitary Cuban personnel are expected to arrive, however. Cuba and Ethiopia signed a public health agreement last month. Some 15 to 20 Cuban medical personnel reportedly are already working with the Ethiopian militia, and another 100 to 150 are expected in the near future. Additional Cuban assistance is also likely in such areas as housing construction and political indoctrination techniques.

The Ethiopian leadership apparently sees the Cuban advisers as most useful in helping with familiarization with new Soviet weapons, establishing training programs, and meeting logistic needs. These needs will become increasingly pressing as more Soviet equipment arrives and the Ethiopian military begins to convert from US equipment.

[redacted] the government does not plan to have Cuban advisers with militia units when they are sent into the field or to have them play a more active training role with either the militia or regular troops. 25X1

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[redacted] the militia forces at the Siga Mega camp north of Addis Ababa now number 100,000. Training is slightly behind schedule, but the government apparently hopes to begin sending men to the field in another month. 25X1

Initially, the government apparently will send most of the militia to Hararge and Sidamo provinces, where the security situation has recently deteriorated. Some militia units may also be sent to Eritrea, probably in order to free regular troops from garrison duty. Despite its large size, the Peoples Militia is unlikely to be an effective fighting force, given the low caliber of its personnel and the haste with which it was organized and

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Divorce and Politics in Brazil

A congressional decision last week to permit divorce in Brazil is likely to add to already serious political strains between church and state in the world's largest Catholic nation. It is also certain to have major social consequences.

The approval of a constitutional amendment to allow divorce for couples legally separated for three years or living apart for five years is a direct consequence of a decree issued by President Geisel earlier this year. Geisel's decree specifies that constitutional amendments need only a simple majority for passage instead of the two thirds previously required. That move, however, was taken in angry response to the defeat of an administration bill to reform the judiciary, and it is unlikely that Geisel anticipated the far-reaching implications of his action.

Even though Geisel--Brazil's first Protestant chief of state--had indicated previously that he was neutral on the issue of divorce, it seemed unlikely that such a measure would ever gain sufficient backing. Indeed, the bill's sponsor, opposition Senator Nelson Carneiro, had been trying for almost 30 years to get such a law enacted.

The fact that his initiative received almost no advance publicity suggests that it was a carefully conceived move by the opposition party to retaliate against the amendment decree and other recent authoritarian moves by Geisel intended to strip the party of its growing influence.

Until now, the military government's principal difficulties with the Brazilian Catholic Church have been with liberal elements that have frequently taken strong public stands against the torture of political prisoners and human rights issues. Now, however, the conservative clergy are also outraged and have asserted that the divorce measure will weaken the institution of the family and lead to degeneracy.

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According to press reports, there are believed to be more than seven million people in Brazil, including some cabinet ministers and military leaders, who consider themselves "married" to second wives or husbands but who, because of the ban on divorce, are still legally wed to their original spouses.

A rush to the civil courts to change marital status will certainly not be the only social consequence of the new law. Within the past week, there have been indications that family planning, previously a "taboo" subject, will soon receive serious attention in a nation that is experiencing severe population pressures.

The lifting of the two-thirds rule for passage of constitutional amendments will probably have further unanticipated consequences, since there are likely to be other controversial legislative proposals that will now have a smoother road to enactment. 25X1

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Bolivia: More Positive Developments for Drug Control

Bolivian coca producers are reportedly responding favorably to "Operation Registration," the government's initial step in its proposed campaign to control the manufacture, smuggling, and consumption of cocaine. *Campesino* leaders, fearful of losing their traditional and lucrative crop, at first voiced opposition to the government's efforts to register coca farmers. But the government's information campaign, designed to explain the motives of "Operation Registration" and the goals of the proposed crop substitution program, apparently has allayed many of the *campesino's* fears.

An increasing number of Bolivian officials are becoming convinced that without adequate control of coca production, it will be impossible to have effective operations against cocaine trafficking. At the same time, the government is hopeful that reducing the *campesino's* dependence on a single crop will stimulate agricultural development and produce other economic benefits.

On the enforcement side, cooperation between Bolivia's Department of Narcotics and Dangerous Substances (DNSP) and the US Drug Enforcement Administration office in La Paz have been strengthened by the signing of an "Agreement of Reciprocal Cooperation." Among other things, the agreement calls for joint planning and coordination of operations and the establishment of a more efficient system of information-sharing between the two drug control institutions.

A great deal of work remains to be done, however, before more effective drug control can be undertaken in Bolivia. A truly cohesive drug control program has not yet been formulated. Moreover, even if such a program were developed, the relative political autonomy of the Santa Cruz region--where perhaps most of the coca is grown--would make La Paz' regulation of crop substitution a difficult task.

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[redacted] 25X6 It is encouraging, [redacted] that the Bolivian government is maintaining an interest and is continuing to take even small measures toward solving the complex narcotics problem.

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Surinam: Soviet Aid Offer

The USSR recently offered Surinam technical assistance for a hydroelectric project, marking the first known economic-related contact between the two countries. Although the Soviets have no permanent diplomatic representation in Surinam, the Soviet ambassador to Colombia and his commercial attache recently arrived in Paramaribo for a four-day visit. The Soviet ambassador presented his credentials during his first visit to Surinam last January.

Surinam reportedly is very interested in establishing trade relations with the USSR, and hopes to exchange its agricultural products for Soviet equipment and machinery. Surinam is known to be having difficulty financing its planned multimillion dollar Kabalebo hydroelectric project near the Guyana border. It is believed, however, that Surinam will proceed slowly on the Soviet offer of development assistance.

The USSR has been seeking closer economic ties with countries in northern Latin America. Moscow signed a preliminary accord in March with Costa Rica for participation in a hydroelectric-aluminum complex. During May, Moscow agreed to supply Mexico with $7 million worth of electrical transformers and signed a framework agreement with Guyana for fisheries cooperation.

In recent years, the Soviet Union has been trying to cut its trade deficits within the region--topping $850 million in 1976. The most successful sales program has been Soviet assistance in the Latin American power industries--providing equipment, machinery, and technical expertise on credit, in hopes of encouraging Latin American purchases to cut the Soviet deficit. Moscow is providing $275 million in aid and technical assistance for power projects in several Latin American countries, including Argentina and Brazil, and is negotiating for participation in several other projects.

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